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China - Peoples Republic of

Cotton and Products Update

China's Cotton Policies drive MY15/16 Cotton Production and Cotton Imports to plummet

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Report Highlights:
As China continues to hold over half the world's cotton in reserved stocks, China's MY15/16 cotton imports are forecast to plummet to 1.25 million tons from the 1.8 million tons in the previous year. This is the lowest level of imports since China joined the World Trade Organization in 2001. The import plunge is mainly due to China's limited issuance of additional import quotas (TRQ) driving the Chinese industry to use imported cotton yarn. MY15/16 cotton production is forecast to hit record low at 5.3 million tons since MY05/06 due to 21 percent fall in planted area in response to the lower government's price support for cotton planting. The forecast MY15/16 for cotton use remains unchanged from the previous year at 7.4 million tons. Meanwhile, China's growing demand for yarn continues to encourage yarn imports.

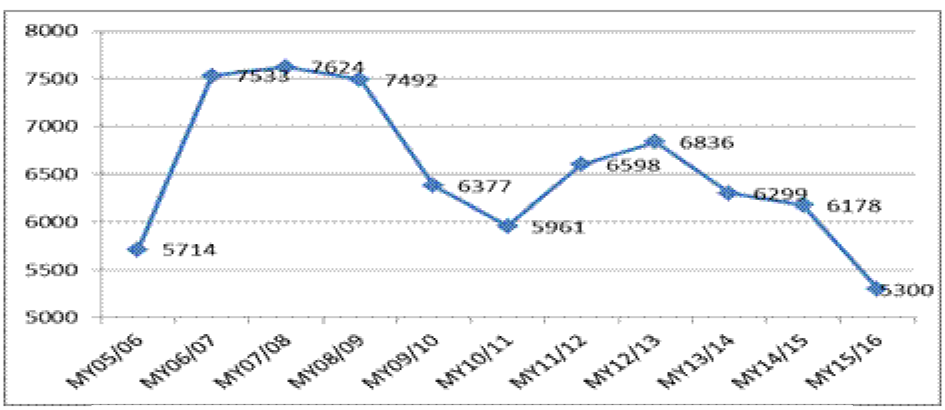
Executive Summary:

As China continues to hold over half the world's cotton in reserved stocks, China's MY15/16 cotton imports are forecast to plummet to 1.25 million tons from the 1.8 million tons in the previous year. The lowest level of imports since China joined the World Trade Organization in 2001. The import plunge is mainly due to China's limited issuance of additional import quotas (TRQ) driving the Chinese industry to use imported cotton yarn. MY15/16 cotton production is forecast to hit record low at 5.3 million tons since MY05/06 due to 21 percent fall in planted area in response to the lower government's price support for cotton planting. The forecast MY15/16 for cotton use remains unchanged from the previous year at 7.4 million tons. Meanwhile, China's growing demand for yarn continues to encourage yarn imports.

MY15/16 Domestic Cotton Production hits lowest level in ten years at 5.3 million tons

MY15/16 cotton production is forecast down to 5.3 million tons as a result of a 21 percent fall in planted the cotton planted area. This fall in planting area is in response of the government's support policy change which lowered subsidies to farmers in the Yangtze River and the Yellow River regions. Although the government support policy for Xinjiang remains similar to last year's, MY15/16 cotton planted area in Xinjiang is forecast to be lower than previously estimated.

China's Cotton Production (MY05/06 to MY15/16; in 1,000 tons)



Source: National Statistics Bureau; MY15/16 Post Forecast

China's leading industry sources' forecast for MY15/16 cotton production ranges from 5.22 million tons to 5.01 million tons. In its November report, China Cotton Association (CCA) forecasted MY15/16 cotton production at 5.22 million tons based on planted area at 3.21 million hectares (MHa), 24 percent fall from the previous year. Specifically the planted area for the Yangtze River and the Yellow River regions are 0.55 MHa (down 38.7 percent) and 0.51 MHa (down 47 percent), respectively, over the previous year. Xinjiang planted area is estimated at 2.1 MHa, down 7.9 percent over MY14/15.

MY15/16 production at 5.22 million tons, down 19.7 percent over CCA's estimated production for MY14/15. The Yangtze river production is 0.61 million tons the yellow river production at 0.48 million tons both down 35.6 percent and 50 percent, respectively, over MY14/15. Xinjiang production is estimated at 4.03 million tons, down 9.1 percent over MY14/15.

The above estimate is based on CCA survey among 2,966 cotton farmers/farms in September in thirteen cotton-producing provinces, and the November data was slightly adjusted based on new field updates.

In November, cncotton.com published a similar estimate for MY15/16 cotton production at 5.22 million tons based on planted area at 3.41 MHa. Cncotton.com's data is based on results of a survey conducted in second half of October covering 3,700 farms/households in fifteen cotton-producing provinces.

	Area (1000 Ha)			Yield (Kg/Ha)			Production (1000 Tons)		
	MY15/16	MY14/15	Change %	MY15/16	MY14/15	Change %	MY15/16	MY14/15	Change %
Total	3412	4273	-20.1	1528	1549	-1.4	5216	6621	-21.1
Yellow River	738	1067	-30.8	1215	1283	-5.6	896	1372	-34.7
-Shandong	333	508	-34.4	1210	1237	-2.2	403	629	-35.9
Yangtze River	530	844	-37.2	1041	961	+8.1	551	812	-32.1
-Hubei	197	342	-42.3	867	807	+7.4	171	276	-38.1
Northwest	2100	2317	-9.4	1773	1896	-6.5	3723	4393	-15.3
-Xinjiang	2066	2264	-8.7	1776	1903	-6.7	3669	4309	-14.9

Source: cncotton.com

In mid-November, the Information Center of China National Cotton Exchange made an even lower MY15/16 production estimate at 5.01 million tons, down 20 percent from its 6.29 million estimate for MY14/15 production. The low production data is based on a lower Xinjiang production in anticipation of lower yields as a result of extremely high temperatures during July-August. In addition, cold September temperatures are also impacting crop growth and maturation.

As of this report, cotton harvest has been completed in three cotton-producing regions and marketing is reportedly faster than the previous year. Information from various industry contacts supports a significant fall in planted area in the Yellow River and Yangtze River regions. However, industry sources indicate that cotton remained a relatively high profitable crop in MY14/15. MY15/16 Xinjiang production is likely to be close to 4 million tons, while MY15/16 total domestic cotton production is forecast at 5.3 million tons.

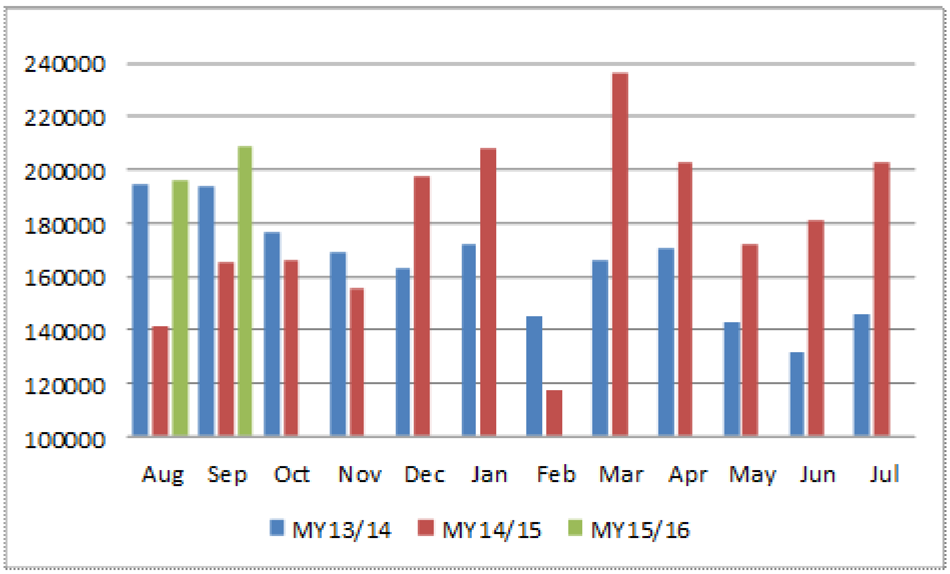
MY15/16 Cotton use remains stagnant at 7.4 million tons

MY15/16 China's cotton consumption is forecast at 7.4 million tons, unchanged from MY14/15. The weak recovery in the demand for textile and apparel products coupled with expected higher imports of yarn tempered China's cotton consumption. China's expected non issuance of additional TRQ for cotton imports outside of the committed 894,000 tons under the World Trade Organization is expected to cut cotton imports and domestic spinning consumption dramatically in MY15/16. Nevertheless, China's estimated GDP and population growth are expected to support moderate growth in cotton fiber use.

MY15/16 Yarn imports expected to increase

Cotton yarn imports remained strong in first two months of MY15/16 at 404,578 tons, up 32 percent over the same period of MY14/15. MY15/16 yarn imports are forecast to grow from the 2.15 million tons in MY14/15. Given that the government has no intention to issue additional TRQs for cotton imports, the current price gap between domestic and international market remains small. This renders imports under full-duty economically unfeasible. Hence, in MY15/16 China's industry will continue to favor the use of more imported yarn instead of using imported cotton to spin yarn. Additionally, the current low price for crude oil will continue to support the use of polyester fiber in yarn production and limit growth in the use of cotton.

China's Monthly Cotton Yarn Imports (MY13/14 to MY15/16; in Tons)



Source: Global Trade Atlas

China's exports of textile and apparel products decreased by 5.4 percent to $234.98 billion in the first ten months of 2015 compared to the previous year, of which apparel exports stood at $143.92 billion, down by 7.5 percent. Industry contacts reported that as a result of China's rise in production costs, orders of textile and apparel products are increasingly shifting to southeast Asian countries.

MY15/16 cotton imports expected to plummet to 1.25 million tons

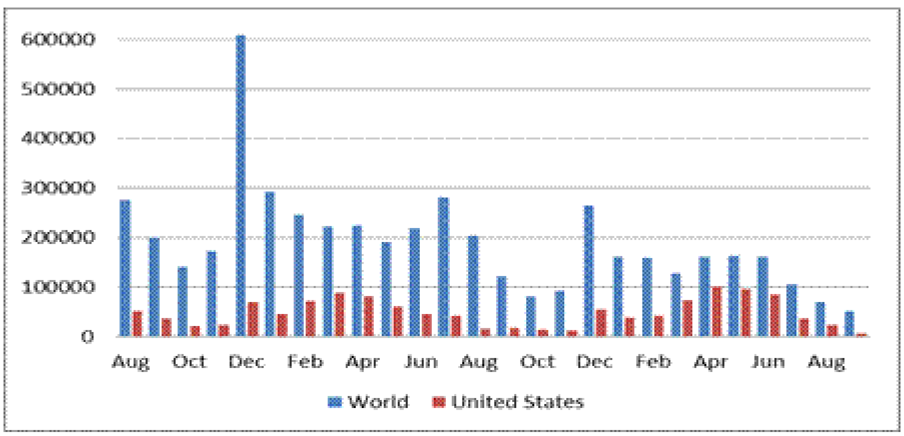
Based on a tight cotton import TRQ, together with an estimated weak recovery in cotton use, MY15/16 cotton imports are forecast to plummet to 1.25 million tons, significantly lower than the

1.8 million tons in MY13/14, and the 3.07 million tons in MY14/15. China's spinners have been requesting the government to add certain TRQ for them to source the grade and quality of cotton from international market to produce the yarn that meets the demand of their customers. However, in consideration of the China's excessive cotton reserves, industry observers indicate that in the near future, the possibility for the government to add any sort of import quota remains very low. Imports of cotton yarn are expected to remain strong and satisfy China's yarn use. Forecast MY15/16 cotton imports by China's industry sources vary and range from 1.25 to 1.65 million tons.

MY15/16 imports from the United States are forecast down from the 587,000 tons in MY14/15. Imports from the United States continued to fall to 29,000 ton in the first two months of MY15/16 compared to 35,000 tons during the same period last year.

It is worth mentioning that the domestic cotton quality deteriorated in recent years as the government's cotton support policy has made yield (rather then quality) the priority for cotton farmers. According to China Fiber Inspection Bureau's inspection results, MY15/16 cotton fiber length averaged 1 mm shorter than the previous year. China's industry leaders continue to advocate for certain additional import TRQs for mills to source higher quality cotton from the global market.

China's Monthly Cotton Imports (MY13/14 to Sep of MY15/16;Tons)



Cotton reserve auctions are expected to re-start

In an effort to reduce the state high cotton reserves and satisfy the textile sector's demand, China is expected to imminently re-start the cotton rotation plan to sell cotton reserves. Industry sources report that the government is doing market research for the next auction. A lower "market-oriented floor price" is likely given that the purchase rate was too low in previous auctions. In addition to the price factor, cotton quality remains the main concerns for domestic spinners. Previous auctions concluded in late August 2015. Out of the 1.85 million tons cotton reserves offered in open auctions, the purchased quantity remained low at 63,413 tons, accounting for merely 3.4 percent.

Cotton area continues to fall?

Based on industry sources, MY15/16 cotton profit remains negative in the Yangtze River and the Yellow River regions. Industry survey indicates cotton farmers could lose RMB8,100/Ha based on

300 working days/Ha at rate of RMB50/working per day/person for cotton farming. In comparison, available informal non-farm jobs in city are offering more attractive wages ranging from RMB100 to 150/day. This makes it unlikely that the cotton area in the Yangtze River and Yellow River regions will stabilize at the current level and likely to fall further in the coming years. As such, Xinjiang is expected to supply 80 percent of the domestic cotton production.

The government's minimum price cotton purchase policy over the past three years achieved high yields at the expense of quality, in particular lower fiber length and macronaire value. In the next few years, the Chinese textile industry will have to use the state cotton reserves which have already experienced an overall decline in quality. In addition, adopting new agronomic practices, and developing varieties suitable for machine harvest will remain challenges for the future of China's cotton production.

Chinese Spinning moving west and abroad

In early 2015, China's State Council published a "Guidance on Promotion of Xinjiang's Employment trough the Development of the Textile and Apparel Industry". The Guidance set up a target for expanding spinning capacity to 12 million spindles during 2015 through 2017 (from the estimated 7 million spindles in 2014), and utilization of 20 percent of Xinjiang cotton production. The total spinning capacity is expected to grow to 18 million spindles by 2020 consuming about 26 percent of Xinjiang cotton. The Guidance also plans to increase Xinjiang's apparel producing capacity to 500 million pieces per year by 2020. The textile and apparel producing chain is expected to create 500,000 to 600,000 jobs for Xinjiang.

In addition, China's high cotton price has significantly reduced its spinning competitiveness and has added costs to its textile and apparel production intended for export. In response, some Chinese spindles have moved to Southeast Asian countries. Similarly, favorable prospects for the Trans-Pacific Partnership (TPP) appear to be also encouraging Chinese spindles to move operations to neighboring countries. For instance, Chinese-invested spindles in Vietnam were estimated at about 2 million in 2014. Chinese textile producers may use yarn from their spinning facilities in southeast Asian countries to get round cotton import TRQs.